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# CUTTING COSTS AND REDUCING REOFFENDING

REDESIGNING PRIVATE PRISON CONTRACTS  
FOR BETTER RESULTS

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# Executive summary

## Key messages

Criminal justice reform is about making communities safer by reducing crime and reoffending, reforming punishment for nonviolent and low risk offenders, and eliminating waste. Focusing scarce resources on violent criminals and recidivists will improve community safety.

Private prisons are responsible for almost one fifth of Australian prison capacity and therefore have a key role in breaking the cycle of offending. Governments can focus private prison operators on this task by tying their profits to their performance in reducing recidivism, measured in simple and absolute terms that are consistent across all prisons and reported publicly.

The goal must be to make rehabilitation and cost reduction integral to the business model of prisons by moving from privatisation to marketisation, so that all prisons (private and public) are subject to competitive pressure regarding their performance in rehabilitating offenders.

## Narrative

Australia has a growing prison population and incarceration rate. This has led to massive costs: \$15 billion annually on criminal justice, including \$4 billion on prisons alone. However, despite this expenditure, almost half of those incarcerated will return to prison within two years of their release. Recidivism is therefore a key driver of the trend towards mass incarceration.

Because some of Australia's largest prisons are privately-operated, there is renewed interest in how private prisons can help solve these problems. Governments have started to innovate in the terms of contracts governing private prisons, with incentives being offered for reduced recidivism and for other outcomes like the delivery of services connected to preventing recidivism. Reducing recidivism will lead to lower criminal justice costs by stopping offenders from cycling through the system. So far, three private prison contracts include recidivism-based performance payments. However, these payments are only a small part of the value of the contracts.

While this is a promising start, there are several factors that will need to be considered for this experiment to succeed. Among these factors are: incentive design, creating a competitive prison system, and allowing prisons more autonomy without compromising safety and community standards. In particular, for performance incentives to be maximally effective, prison operators will need to adopt a different business model, with significantly more of their revenue being performance-dependent. Following the recommendations outlined in this report gives the experiment the best chance of succeeding.

## Findings

- Eight of Australia's 98 prisons are operated by four private companies. These prisons make up an estimated 18 percent of Australia's prison capacity. This figure declined recently as Queensland took back into public hands its two private prisons.
- It is estimated that as a percentage of the prison population, Australia's use of private prisons is the most extensive in the world. However, the sector has grown little over the past 20 years.
- The fees governments pay to prison operators are unknown in seven of the eight cases. Total contract values are known for three more of the private prisons.
- It is known that seven of the eight private prisons are governed by contracts including incentives for service delivery, including safety measures. Three private prison contracts are known to include incentives for reduced recidivism: Parklea in New South Wales, Ravenhall in Victoria, and Melaleuca in Western Australia.
- There is emerging evidence for private prisons operating more cheaply than public prisons. The most recent Australian evidence supports their cost-effectiveness.

## Recommendations

1. Private prison contracts should include strong incentives for reduced recidivism.
2. The goal of redesigning private prison contracts must be to reduce costs over the longer-term.
3. Recidivism incentives should be bonuses rather than penalties, and connected to individual prisoner outcomes, not aggregate performance.
4. Private prison contracts should be structured so that operators cannot make their margins without the recidivism bonuses.
5. Measures for services linked to recidivism should be standardised across prisons within a system to enable comparisons.
6. Results and costs should be publicly reported.
7. Within systemic constraints, prison autonomy should be increased to enable innovation and competition.



## Observations

- Government-set performance targets are difficult for free-market policymakers. The desire to use competition to improve performance and lower costs is in tension with the government taking upon itself the role of shaping what a market produces and in what quantity.
- However, the government's natural monopsony in criminal justice gives it a strong position to negotiate favourable terms. Moreover, incentives for reduced recidivism are simple to design and over time a picture of whether and which prison programs are effective will emerge, allowing the attribution of reward and responsibility for recidivism to prisons.
- The primary reason for supporting incentives for reduced recidivism incentives is the current system is failing. The risk private prisons will make the situation worse if they pursue a reduction in recidivism seems small as against the known outcomes of the current system.
- Targeted reform is needed as an alternative to more radical approaches to addressing the failures of the criminal justice system.

# Introduction

The purpose of this paper is not to rehash the debate about prison privatisation in its entirety. Private prisons have operated in Australia since 1990, and Australia has had, in world terms, a consistently high proportion of prisoners in private prisons for 20 years. A new private prison, Ravenhall, opened in Victoria in 2018, and the new private prison, Clarence Correctional Centre, in Grafton, New South Wales will be the largest prison in Australia when it opens in 2020.<sup>1</sup> The South Australian Government has also announced plans to privatise the new Adelaide Remand Centre in 2019.<sup>2</sup> While data is mixed as to the cost and effectiveness of private prisons, and although Queensland recently took back control of its two private prisons, they are and will continue to be a key part of Australia's prison systems.<sup>3</sup>

Instead, this paper discusses prison privatisation as a potential tool for governments seeking to address Australia's high levels of recidivism, which contributes to the rising levels of incarceration and criminal justice spending across the country.<sup>4</sup> To make this point clear: our interest in private prisons is in their potential to contribute to a lower-cost, more effective criminal justice system in which repeat offending is reduced.

The reform discussed in this paper should be seen in the context of Australia's underperforming criminal justice system. Australia has a rapidly growing prison population: the prison population has grown by 38 percent in the last five years, far outstripping overall population growth. There are more than 43,000 people in Australian prisons.<sup>5</sup> The imprisonment rate increased from 166.9 per 100,000 adults in 2008-09 to 216.8 per 100,000 adults in 2017-18.<sup>6</sup> But our prison system is failing to correct the behaviour of many offenders. Nationally, 58 percent of sentenced prisoners have been in prison before.<sup>7</sup> In 2016-17, 45 percent of adults released from prison returned to prison within two years, and 53 percent returned to the criminal justice system within two years. These figures have risen in the last five years.<sup>8</sup>

At the same time, Australia is spending more and more on incarceration. Prisons are expensive. Australia spends more than \$4 billion on corrective services, most of which

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1 GEO Group Australia, "Ravenhall correctional centre: world-leading continuum of care," accessed 22 January 2019. <https://www.geogroup.com.au/ravenhall-correctional-centre.html> Grafton Serco, "Home page," accessed 22 January 2019. <https://griftonserco.com.au/>

2 Simon Evans, "British giant G4S eyes South Australian prison outsourcing contract," *Australian Financial Review*, 5 September 2018, accessed 11 February 2019. <https://www.afr.com/business/infrastructure/british-giant-g4s-eyes-south-australian-prison-outsourcing-contract-20180905-h14yap>

3 Melanie Vujkovic, "Queensland government to run privately owned prisons in bid to reduce assaults," ABC News, 26 March 2019, accessed 16 April 2019. <https://www.abc.net.au/news/2019-03-26/queensland-private-prisons-to-be-run-by-state-government/10938192>

4 A note on terminology: this paper uses the word 'recidivism' to capture both 'reoffending', meaning an offender who is convicted of another crime subsequent to incarceration, and 'reincarceration', meaning an offender who returns to prison subsequent to incarceration. Where used, 'reoffending' should be read with this specific meaning in mind.

5 Australian Bureau of Statistics, *Corrective Services Australia*, September 2018

6 Productivity Commission, *Report on Government Services 2019* Table 8A.5

7 Australian Bureau of Statistics. *Prisoners in Australia 2018* Table 9

8 Productivity Commission, as above, Table CA.4

goes to prisons. This represents more than a quarter of all spending on justice (police, courts, and punishment). Spending has grown at 4 percent per annum over the last five years.<sup>9</sup> A previous IPA research paper found that Australian prisons are the 5th most expensive in the developed world on a per prisoner per year basis.<sup>10</sup>

In the United States, conservative states like Texas and Georgia have shown that it is possible to safely reduce incarceration and lower costs by reforming punishment for nonviolent offenders and by concentrating prison resources on rehabilitation.<sup>11</sup>

It is not surprising, then, that governments have become interested both in how prisons might become more effective in reducing recidivism and in how private prisoner operators might be incentivised to make rehabilitation a priority. In particular, there have been innovations in the terms of operator contracts, with new performance payments targeting reduced recidivism. Ravenhall's contract includes an incentive for outperforming the rest of the system.<sup>12</sup> The new Melaleuca women's prison in Western Australia pays the operators a bonus for each released prisoner who does not return to the system within two years.<sup>13</sup>

These are promising steps. But the effort to integrate reduced recidivism into the remit of private prisons will not be successful unless a number of weaknesses in the measures used, data sharing and transparency, and system design are addressed.

This paper discusses what should be done to increase the chances that this reform will be a success. It also discusses well-known reservations about private prisons and government-set performance targets. It argues that these issues notwithstanding, there is nonetheless a sound case for pursuing this reform.

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9 *Ibid* Table CA.1

10 Andrew Bushnell, *Australia's criminal justice costs: an international comparison*, Institute of Public Affairs, December 2017

11 Andrew Bushnell, *Criminal justice reform: lessons from the United States*, Institute of Public Affairs, April 2017

12 Partnerships Victoria. *Project summary: Partnerships Victoria Ravenhall Prison Project*, February 2015. <https://www.dtf.vic.gov.au/partnerships-victoria-ppp-projects/ravenhall-prison-project>

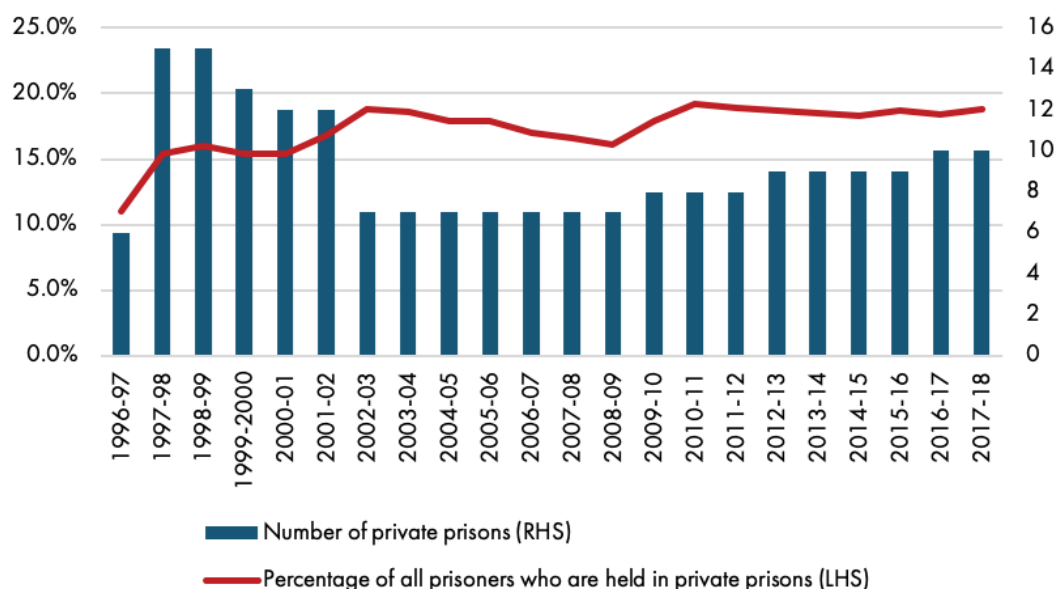
13 Courtney Bembridge, "New Perth women's prison opens with cash incentives for successful rehab" ABC News 18 December 2016, accessed 22 January 2019 <https://www.abc.net.au/news/2016-12-18/new-womens-prison-opens-in-perth-with-operator-offered-incentive/8130394>

# 1. Key facts: private prisons in Australia

## 1-1. Overview of private prisons and operators

The first private prison in Australia opened in 1990. The operation of Borallon Correctional Centre in Queensland was privatised soon after construction by the state. The Queensland Government was looking to reduce costs and inject competition into the prison system.<sup>14</sup> Over the course of the 1990s, the idea spread to other states. As Figure 1 shows, by 1997-98 there were 15 private prisons around the country, holding 15.4% of the nation's prisoners.

**Figure 1: Private prisons in Australia over the last 20 years**



Source: Productivity Commission, *Report on Government Services* (each year from 1999 onwards)

Since then, the number of private prisons has declined. As recently as 2008-9, there were only seven private prisons in Australia. In 2017-18 there were 10 private prisons, and as noted this has now declined to eight. The percentage of prisoners who are housed in private prison rose slightly, from 15.4 percent in 1997-98 to 18.4 percent in 2016-17.

A 2013 study by The Sentencing Project found that Australia has, on one measure, the most widespread use of private prisons in the world. At the time, 19 percent of prisoners were held in private prisons, a greater share than any other country. By contrast, the United States has the most prisoners in private facilities in absolute terms but these prisoners only make up eight percent of the prison population.<sup>15</sup>

<sup>14</sup> Richard Harding, "Prison privatisation in Australia: a glimpse of the future" *Current Issues in Criminal Justice* 4(1) 1992. Available here: <http://classic.austlii.edu.au/au/journals/CICrimJust/1992/20.html>

<sup>15</sup> Cody Mason, *International growth trends in prison privatization*, The Sentencing Project, 20 August 2013. Available here: <http://www.sentencingproject.org/publications/international-growth-trends-in-prison-privatization/>



Until recently, there were private prisons in each of the five mainland states. The percentage of prisoners held in private prisons ranges from 13 percent in New South Wales to 31 percent in Victoria. This is summarised in Table 1 below. Queensland's formerly privately operated prisons are included for completeness.

**Table 1: Private prisons by jurisdiction**

Jurisdiction	Number of private prisons	2017-18 prisoner share
New South Wales	2	13.4%
Victoria	3	31.2%
Queensland	2*	17.9%
Western Australia	2	25.7%
South Australia	1	16.4%

Source: Productivity Commission, *Report on Government Services 2019*, Tables 8A.3 and 8A.4

\*But see fn 3 above.

The eight private prisons are controlled by five contractors: American company GEO, British companies G4S and Serco, and French company Sodexo, and from April 2019, the international consortium MTC-Broadspectrum, which now operates Parklea. All have operations in several countries and diverse interests. In Australia, GEO is the market leader in terms of prison capacity, but is expected to be overtaken by Serco when Clarence comes on line in 2020. This is summarized in Table 2 below.

**Table 2: Private prisons by operator – as at August 2019**

Company	Number of prisons	Total capacity (beds)	Share of private prisoners
GEO	3	2983	41%
G4S	2	1580	22%
Serco	1	1513	21%
MTC-Broadspectrum	1	1000	14%
Sodexo	1	254	3%

At the time of writing, GEO controls one prison in New South Wales and two in Victoria. G4S has prisons in Victoria and South Australia. Serco and Sodexo's only prisons are in Western Australia. Only Victoria and Western Australia have two operators in control of facilities. Two observations follow: first, that no company dominates any state market when compared to the system as a whole; but second, there is little competition between providers in state markets beyond the tender stage.

## 1-2. Private prison contract details

With recidivism becoming a key focus in the prison system, it is important to consider available information about the contracts governing private prisons. Unfortunately, this information is not always made public. The available information about the eight private prisons is compiled in Table 3, along with the two formerly private prisons in Queensland.

The table reveals that three prisons, Ravenhall, Parklea, and Melaleuca, currently have contracts that are known to include incentive payments for reduced recidivism. Of the seven prisons for which the information was available, all had contracts including penalties for poor prison management, including incidences of suicides, riots, and positive drug tests. The two private prisons in Queensland were originally put out for tender but as noted the Queensland government decided instead to take control of the states' private prisons from June 2019 following an investigation by the Crime and Corruption Commission into corruption risks across Queensland corrective facilities.<sup>16</sup> Queensland has never made prison contracts publicly available. The value of the contracts that are in place is not widely known, with figures available for only three of the prisons.

### The new contract for Parklea prison

In April 2019, Parklea prison in New South Wales was taken over by a new consortium, MTC-Broadspectrum. The Commissioner of Corrective Services New South Wales, Peter Severin, told the NSW Legislative Council in 2018 that "The new contract is intended to provide greater comparability between publicly and privately managed prisons and a more transparent picture of performance across the prison system in order to ensure community safety and reduce the rate of reoffending".<sup>17</sup>

The new contract includes an extensive performance regime comprising 25 Key Performance Indicators, with a points system determining their effect on the performance component of the monthly service payment, and four charge events that lead to direct penalties. The contract also includes monthly reintegration payments that cover the costs of reintegration services and an annual incentive payment for a reduction in reincarceration, measured against a benchmark year. The payments are capped.<sup>18</sup>

The previous contract for Parklea (with GEO) was criticised for its lack of transparency.<sup>19</sup> The new contract is similarly secretive about the level of payments, with the sections that provide examples of how performance payments work in practice being redacted.<sup>20</sup> Transparency is discussed in Section 3-2-1 of this report.

16 Advice received by private correspondence from Queensland Corrective Services, 12 March 2019. Information on the investigation, known as Taskforce Flaxton, can be found here: <http://www.ccc.qld.gov.au/corruption/taskforce-flaxton/taskforce-flaxton-an-examination-of-corruption-risks-in-corrective-services-facilities>

17 Portfolio Committee No. 4 – Legal Affairs, *Parklea Correctional Centre and other operational issues*, NSW Legislative Council, December 2018 p. 44 Available here: <https://www.parliament.nsw.gov.au/lcdocs/inquiries/2470/Report%20No%2038%20-%20Parklea%20Correctional%20Centre%20and%20other%20operational%20issues.pdf>

18 Corrective Services NSW, "Class 3 contract documents awarded tenders," accessed 22 January 2019. [https://www.correctiveservices.justice.nsw.gov.au/Pages/CorrectiveServices/related-links/doing-business-with-csnew/class\\_3\\_contract\\_documents.aspx](https://www.correctiveservices.justice.nsw.gov.au/Pages/CorrectiveServices/related-links/doing-business-with-csnew/class_3_contract_documents.aspx)

19 Portfolio Committee No. 4- Legal Affairs, as above, pp. 45-8

20 Corrective Services NSW, "Class 3 contract documents awarded tenders," as above, all annexures to Schedule 10 are redacted

**Table 3: Governance of private prisons**

Prison	Type	Capacity	Operator	Fees	Operations incentives?	Recidivism incentives?	Fees public?
New South Wales							
June	Min-med	790 (men)	GEO	Operational fee Performance fee	YES	NO	NO Value: \$749m over 15 years
Parklea	Min, max	1000+ (men)	MTC (from April 2019)	Operational fee Performance fee	YES	YES (from April 2019)	NO Contract value: \$90m p.a.
Victoria							
Fulham	Med	893 (men)	GEO	Prisoner place fee Services fee	YES	NO	NO
Port Phillip	Max	1087 (men)	G4S	Prisoner place fee Services fee	YES	NO	NO 3.11b nominal value over 20 years
Ravenhall	Med	1300 (men)	GEO	Prisoner place fee Services fee	YES	YES 2.5% of service fee linked to out-performing system on reoffending	NO Projected cost: 6.3b over 25 years
Queensland*							
Arthur Gorrie	Max	1000+ (men)	GEO	Prisoner place fee (details N/A)	N/A	N/A	NO
SQCC	Min-max	300 (men)	Serco	N/A	N/A	N/A	N/A
South Australia							
Mount Gambier	Min-med	493 (men)	G4S	Per prisoner fee	YES	NO	NO
Western Australia							
Acacia	Med	1513 (men)	Serco	Operational fee Performance fee (% of op fee)	YES	NO	YES
Melaleuca	Max	254 (women)	Sodexo	N/A	N/A	YES \$15k bonus per non-reoffender	NO

Sources for this table are listed in a designated section in the bibliography.

Explanatory note: 'Operations incentives' are generally penalties for events like deaths in custody, escapes, and riots, and penalties tied to indicators like the rate of positive drug tests, and proportions of eligible prisoners enrolled in education and training.

\*As noted these prisons are now operated by Queensland Corrective Services.

### 1-3. Private prisons' record on costs

There is emerging evidence for private prisons operating more cheaply than public prisons. Two recent independent reviews of private prisons in Victoria and Queensland found that they generate substantial savings for those states, estimated at up to 20 percent in Victoria and \$55 million between 2008 and 2014 for Queensland taxpayers.<sup>21</sup> At the time of signing a new contract with Serco for the operation of Acacia Prison, the Western Australian Government claimed the contract would save taxpayers \$55 million over five years, without affecting service standards for prisoners. It is also worth noting that the Queensland government estimates its decision to take over the operation of the states two private prisons will cost taxpayers and extra \$111 million over four years.<sup>22</sup>

Sydney University researchers Jane Andrew, Max Baker, and Phillip Roberts raise questions about how private prison operating costs are calculated, including whether government overheads are included. They note that it is hard to come to a definite judgement without greater transparency about operating costs and contractual terms. For this reason, they dispute earlier findings in New South Wales and Queensland that private prisons save taxpayers money.<sup>23</sup> However, as United Kingdom expert Julian Le Vay makes clear it is not always appropriate to include public sector overheads in estimates of private prison savings, as Andrew *et al* insist.<sup>24</sup> If a department of corrections fails to reduce its overheads following privatisation, say by not reducing its staffing levels, the private provider cannot fairly be held responsible for this. In comparing the costs of private and public prisons, both marginal and full accounting is required.

International evidence for lower costs is mixed, but mostly positive. In the United States, Volokh finds that while the evidence that private prisons have reduced costs in that country is mixed, the best studies do show a saving.<sup>25</sup> In the UK, Le Vay estimates that private prisons may operate more cheaply by as much as 30 percent.<sup>26</sup>

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21 Victorian Auditor General's Office, as above, pp. 83-9 Queensland Audit Office, as above, pp. 1-6

22 Vujkovic, as above

23 Jane Andrew, Max Baker and Phillip Roberts, *Prison privatisation in Australia: the state of the nation*, The University of Sydney Business School, 2016. Available here: [https://business.sydney.edu.au/\\_\\_data/assets/pdf\\_file/0008/269972/Prison\\_Privatisation\\_in\\_Australia-The\\_State\\_of\\_the\\_Nation\\_June\\_2016.pdf](https://business.sydney.edu.au/__data/assets/pdf_file/0008/269972/Prison_Privatisation_in_Australia-The_State_of_the_Nation_June_2016.pdf) pp. 15-16 and p. 25

24 Julian Le Vay, *Competition for prisons: public or private?*, Bristol University Press, Policy Press, 2016, p. 160

25 Volokh, as above, pp. 357-360 and Alexander (Sasha) Volokh, "Don't end private prisons," *Washington Post*, 19 August 2016, accessed 12 February 2019. <https://www.washingtonpost.com/news/volokh-conspiracy/wp/2016/08/19/dont-end-federal-private-prisons/>

26 Le Vay, as above, p. 255

It is often argued that private prisons' lower costs come at the expense of prison conditions. It must be acknowledged that there have been instances of standards becoming unacceptable in private prisons in Australia. In recent years, Arthur Gorrie, Parklea, and Melaleuca have all attracted the attention of authorities and media.<sup>27</sup> The overall finding, however, may differ from these specific instances. There is some evidence that the introduction of private prisons into a public system contributes to higher standard across the board. This was cited by the Western Australian Economic Regulation Authority in its review of that state's prisons.<sup>28</sup> Australian academic Richard Harding also argues for the possibility of "cross-fertilisation" between public and private prisons, and cites examples from the US, UK, and Australia.<sup>29</sup>

There is therefore good reason to be positive about the connection between private prisons and lower-cost delivery of prison services. The question at hand, then, is how to combine these advantages with a focus on reducing reoffending, so that the aggregate costs of criminal justice over the longer term are reduced.

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27 Mark Willacy and Alexandra Blucher, "Inside Australia's 'powder keg' private prison," ABC News, 20 June 2018, accessed 11 February 2019. <https://www.abc.net.au/news/2018-06-20/inside-arthur-gorrie-correctional-centre/9837260> The Feed SBS, "Inside Parklea: the deadly consequences of Australia's private prison boom," 20 November 2018, accessed 23 January 2019. <https://www.sbs.com.au/news/the-feed/inside-parklea-the-deadly-consequences-of-australia-s-private-prison-boom> See also fn 49, above, regarding Melaleuca.

28 Economic Regulation Authority, as above, p. 235 and p. 242 (pointing to the introduction of the Inspector of Custodial Services which provides independent oversight of the system).

29 Harding (2001) "Private prisons" *Crime and justice* 28 pp.265-346, pp. 331-6



## 2. Incentive design

**Recommendation 1:** Private prison contracts should include strong incentives for reduced recidivism.

With recidivism a major driver of Australia's rising incarceration rate and associated costs, private prisons should be incentivised to pursue more effective rehabilitation of prisoners. Private prisons can be incentivised towards reducing recidivism rates directly, through an incentive (whether a bonus or a penalty) tied to a specific measure, or indirectly, where the incentive is connected to the delivery of services correlated with reduced recidivism, like education, skills training, and healthcare provision. This section discusses direct recidivism incentives. Indirect incentives are discussed in Section 3-1 below.

In recent years, governments in Australia and in other countries have started to include direct incentives for reducing recidivism in the contracts governing private prisons. This is a welcome trend, and should be pursued by governments, subject to the observations in Section 4, below. As part of the criminal justice system, prisons have several functions, including the incapacitation of criminals, the punishment of criminals as integral to the vindication of individual rights and social norms, the deterrence of crime, and the rehabilitation of criminals (as measured by their rates of return to criminal activity following incarceration). At the moment, most private prison contracts are based on delivering the first three of these goods at lower cost than state-run prisons, but states are now taking seriously the possibility that private prison operators can also be engaged to deliver the fourth of these priorities as well.

So far, there are three Australian private prisons with such incentives, with one more set to commence operation in 2020:

- The contract for Victoria's Ravenhall prison, signed in 2015, provides for a performance payment if it outperforms other prisons in reducing reoffending. The payment could be as high as \$2 million per year.<sup>30</sup> However, the total payment over the 20-year contract is expected to be \$3.11 billion (nominal undiscounted cost).<sup>31</sup> Projects Victoria describes the performance payment as a "small component" of the fees paid.<sup>32</sup>

30 Nino Bucci, "Victoria's Ravenhall prison operators to be paid up to \$2 million bonus if reoffending reduced" *Sydney Morning Herald*, 12 February 2015, accessed 11 February 2019. <https://www.smh.com.au/national/victorias-ravenhall-prison-operators-to-be-paid-up-to-2-million-bonus-if-reoffending-reduced-20150212-13d8gb.html>

31 Minister for Corrections, "Victoria extends Port Phillip Prison contract," Media release, 11 January 2016, accessed 11 February 2019. <https://www.premier.vic.gov.au/victoria-extends-port-philip-prison-contract/>

32 Department of Treasury and Finance, "Project summary – Partnerships Victoria Ravenhall Prison Project," accessed 11 February 2019. <https://www.dtf.vic.gov.au/sites/default/files/2018-01/Ravenhall-Prison-Project-Summary-February-2015.pdf> p. 25

- The Melaleuca Remand and Reintegration Facility in Western Australia is run by Serco, which will reportedly receive a \$15,000 bonus for each released prisoner who does not reoffend within two years of release.<sup>33</sup>
- The new contract for Parklea with MTC-Broadspectrum includes a complex performance payment scheme (as described in Section 1).
- The new prison at Grafton, New South Wales, which is set to open in 2020, will also be incentivised to reduce recidivism. Operators will be able to earn annual incentive payments for reducing reoffending among four different cohorts: indigenous males, non-indigenous males, indigenous females, non-indigenous females. The available project description does not detail the measure or scale of the payments.<sup>34</sup>

Australia is not unique in pursuing this innovation. Notable overseas examples include:

- Auckland South Correctional Facility, also known as Wiri after the suburb in which it is located, is run by a private consortium. Its contract includes incentive payments for reducing recidivism by released prisoners.<sup>35</sup> This goal was incorporated into even the construction of the facility, which is designed so that prisoners demonstrating good behaviour can be rewarded by moving closer to the facility's gate, and from a row to a residence.<sup>36</sup>
- The United Kingdom government ran two reoffending reduction pilot programs in prisons at Peterborough and Doncaster. The two trials tested different models, with Peterborough being based on a Social Impact Bond model that delivered a return to investors upon targets being met. Members of the Peterborough cohort were reconvicted 8.4 percent less than a matched national control group, which was enough to earn the bonus but short of the government's 10 percent target.<sup>37</sup> Results at Doncaster were less promising. Service provider Serco was charged with reducing reconviction rates for the cohort by five percent or more or else its payment would be reduced. The first cohort was reconvicted 5.7 percent less than the 2009 baseline that was used (note that this is a different measure than the one at Peterborough). The second cohort was reconvicted only 3.3 percent less than the baseline.

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33 Courtney Bembridge (2016) "New Perth women's prison opens with cash incentives for successful rehab" ABC News 18 December 2016, accessed 22 January 2019. <https://www.abc.net.au/news/2016-12-18/new-womens-prison-opens-in-perth-with-operator-offered-incentive/8130394>

34 NSW Treasury, *Project Summary: New Grafton Correctional Centre*, accessed 12 February 2019. <https://www.treasury.nsw.gov.au/sites/default/files/2017-09/New%20Grafton%20Correctional%20Centre%20-%20Project%20Summary.pdf>

35 The complex formulas for the incentives payments are outlined in Schedule 16 of the governing contract. Department of Corrections, "The contract," accessed 12 February 2019. [https://www.corrections.govt.nz/about\\_us/getting\\_in\\_touch/our\\_locations/auckland\\_south\\_corrections\\_facility/contract.html](https://www.corrections.govt.nz/about_us/getting_in_touch/our_locations/auckland_south_corrections_facility/contract.html)

36 Rikha Sharma Rani, "New Zealand tries a different kind of prison," *Citylab*, 1 September 2017, accessed 12 February 2019. <https://www.citylab.com/equity/2017/08/new-zealand-tries-a-different-kind-of-private-prison/538506/>

37 The final results of the trials can be found here: Ministry of Justice, "Final results for cohorts 1 payment-by-results prison pilots," accessed 12 February 2019. <https://www.gov.uk/government/statistics/final-results-for-cohorts-1-payment-by-results-prison-pilots>

- A more tangential but still worthwhile example: in 2013, Philadelphia cancelled all of its contracts for privately-run community corrections facilities. The contracts were rewritten to include performance incentives related to reduced recidivism. In the following two years, the halfway house system saw an 11.3 percent reduction in recidivism.<sup>38</sup>

As these examples demonstrate, there have been a variety of approaches taken to creating direct recidivism incentives. It should be noted that while ‘reoffending’ has been the most common standard used for measuring performance, it would be possible to use the narrower standard of ‘reincarceration’, meaning that the incentives could be tied to released prisoners not returning to prison (as opposed to not offending at all). There are good reasons to prefer some of these approaches to others.

**Recommendation 2:** The goal of redesigning private prison contracts must be to reduce costs over the longer-term.

One of the challenges of privatisation is that the terms offered to contractors must be sufficiently attractive to create competition in the supply of the service in question, but not so generous that taxpayers end up paying more for the service than they would otherwise. In the case of incentive payments for reduced recidivism, this dynamic may result in a short-term increase in costs if private prisons succeed in developing effective innovations in rehabilitation. However, such a spike in payments would be offset by reduced downstream costs as the system is less burdened by policing, prosecuting, and punishing repeat offenders. This is the same logic as ‘justice reinvestment’, which is the policy of redirecting money allotted to incarceration to rehabilitation, on the premise of reducing longer-term costs through more effective corrections. Any proper accounting of private prisons’ value for money would need to take this into account.

That said, this cost-benefit analysis does create a constraint on the negotiating positions of both parties. Governments must be mindful that performance payments must be linked to objectives that are inextricably connected to lower longer-term costs. This may affect, for example, whether the metric used is reoffending or reincarceration.

**Recommendation 3:** Recidivism incentives should be bonuses rather than penalties, and connected to individual prisoner outcomes, not aggregate performance.

There are two key points to make about these approaches to incentive design, the first going to the psychology of the incentive, the second going to the metric used to determine success.

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<sup>38</sup> Leonard Gilroy, “Pay for success contracting reducing recidivism in Pennsylvania,” *Reason*, 31 August 2015, accessed 12 February 2019. <https://reason.org/commentary/pennsylvania-contract-recidivism/>

The Ravenhall contract effectively creates a penalty for not reducing recidivism: the operator must hit the target to receive the quarterly payment in full. Conversely, the Melaleuca contract pays a bonus. The new Parklea prison contract imposes penalties for underperformance against KPIs as well as incentive payments specifically for reducing reincarceration.

As Alexander Volokh points out, in accounting terms, there is no difference between bonuses and penalties. Whether a contract offers a reward or imposes a penalty, provided they are the same amount, the effect on the behaviour of the bidding company will also be the same because its own projections of its performance will not change. That is, if the contract specifies a bonus, then bidders will compete by reducing their base rate demands by the value of whatever level of bonus they project they will earn; whereas if the incentive is a penalty then bidders will require a higher base rate and factor in their anticipated penalties. In both cases, they will act based on how much they need to earn to achieve their desired profit margin.<sup>39</sup>

However, Volokh notes, this does not take into consideration insights from behavioural economics. Prospect theory suggests that actors are more aggressive in trying to avoid losses than in trying to maximise gains; where actors have hit their targets, whatever they may be, they become risk averse, whereas if they are still chasing their targets they are risk-seeking. While this might seem at first to suggest a penalty would be the best incentive, it actually suggests that bonus payments are the better choice. Under the bonus structure, bidders have (assuming government negotiators know what they are doing) accepted a base rate that is lower than they need to make their margin. Their default position is a loss. As such, per prospect theory, they will be aggressive in trying to achieve their target (that is, their profit margin). Under a penalty structure, the base rate is higher than the sought margin, leading to conservative actions to avoid penalties. Bonuses can therefore be expected to more strongly incentivise innovation. This insight was borne out by the trials in the United Kingdom, where the more successful Peterborough trial paid investors a return for improved performance. This makes some sense intuitively as well. In a normal business, entrepreneurs must invest capital and produce something of value in order to recoup, and surpass, their investments. They start from a position of loss, and assume the risk that they will not succeed. Prison operators should face the same pressure.

The second point is that the metric used to determine the bonus should be simple. One of the key challenges in tying payment to performance is developing workable metrics and baselines. Comparisons of public and private prisons, and of prisons generally, are usually unreliable because of the diversity of circumstances across prisons and the lack of consistent data collection and tracking.<sup>40</sup> A simple standard, like the one at Melaleuca, is easier to track and to comprehensibly report. There is no need for a baseline or comparisons with other prisons: once a prisoner has been in a facility for a

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39 Alexander Volokh, "Prison accountability and performance measures," *Emory Law Journal* Vol. 63 2013 pp. 339-416; Emory Legal Studies Research Paper no. 13-263, p. 377

40 For an overview of these problems in the Australian context, see Andrew, Baker and Roberts, as above. Similar problems are discussed in a US context in Volokh, as above.

certain length of time, his or her outcome is 'owned' by the provider. If he or she stays out of prison, or does not offend, for the stipulated length of time, the operator gets a payment.<sup>41</sup>

This individualised approach has another merit: it accurately conveys where the risks lie. Crime is committed by individuals, and it affects individuals. It is not committed by artificially constructed classes of criminals against other aggregations. Someone assaulted in the street by a released prisoner is not consoled if the prison achieves some aggregate-level target. Such a target creates an asymmetry between the risk taken and the costs and rewards of taking that risk. Put another way: the risk of releasing a criminal operates at the individual level, so the assumption of that risk should operate at the same level. Using aggregate measures allows governments and operators to hide how risk is distributed by the contract. Unless risks taken are accurately attributed to actors, the incentive for those actors learn from their losses and improve accordingly is diminished.<sup>42</sup>

**Recommendation 4:** Private prison contracts should be structured so that operators cannot make their margins without the recidivism bonuses—a new business model for operators.

The above logic, however, only applies where the default position of the operator is a loss. Unless this is the case, the operator cannot be expected to aggressively chase the bonus, and so the expected performance improvement is less likely to eventuate.

In the trial at Peterborough, the recidivism programs were funded by investors. By buying bonds, they had committed capital to the venture, meaning that they had a stake in its success. This is what it means to create symmetry between investment and risk/reward. It should not be the case that where the project fails, it is the taxpayer who loses, but where it succeeds, it is the operator who profits. The chances of both loss and profit need to be owned by the operator.

The situation is complicated by the fact that, as noted above, reducing recidivism is not the only purpose of prisons. Prisons also exist to remove offenders from the community and to punish offenders by depriving them of their liberty. Operators will rightly expect to be paid for these services as well. But where the payment for those services is by itself profitable, this will cut across the logic of incentivising rehabilitation.

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41 It should be noted, however, that the negotiating parties will rely on a benchmark of some sort to arrive at an idea of expected performance. This is necessary to come to an agreement on price. Bidding companies will need to know or estimate what level of bonus or penalty they can expect, and governments will need to know what kind of improvement from the status quo they think they are buying. Under this simple scheme, however, these benchmarks need not be made public, and public reporting will be more intelligible for third parties looking to scrutinise performance—like, for example, civil society groups (including the IPA).

42 As explained in Nassim Taleb, *Skin in the game: hidden asymmetries in daily life*, Random House, 2018.



Any proper performance incentive therefore requires operators to accept a very different business model than they have in the past. The feasibility of expecting operators to accept terms like these are discussed further in Section 4. It should be noted here, though, that the levels of incentive payment that have been accepted by operators so far suggests that this new business model has not yet found favour with them. The Ravenhall contract, for example, includes recidivism payments that constitute just 2.5 percent of their operational payments. This is likely insufficient incentive for reshaping the operation of the prison towards rehabilitation.

However, the possibility of unintended consequences must be considered. Confronted with a contract that is loss-making without the bonuses, private prison operators may drop their interest. This is true if operators believe that the demands of government are unrealistic, such that the bonuses are unattainable. It is unlikely that rehabilitation is entirely within the control of operators. Simply raising the payments on offer will likely not increase the possibility of reforming the behaviour of hardened criminals. Moreover, if operators are discouraged from bidding by unrealistic demands, this would deprive the state of the cost savings that prison privatisation may offer under less stringent conditions (the cost-effectiveness of private prisons is discussed in Section 4-3 below).

Another foreseeable possibility is that prison operators may attempt to reduce service levels to hedge against underperformance in relation to recidivism targets. That is, where prison operators anticipate not being able to achieve sufficient bonuses to make a profit, they will have a strong incentive to reduce their costs (effectively writing off the bonuses). This is also true on a performance penalty model: if operators believed that they would be subject to a certain level of penalty such that their profit margin disappeared, they would be incentivised to cut costs.<sup>43</sup>

For this reason, some measure of prescriptiveness in the governing contracts regarding service levels, beyond obvious requirements like respect for the rights of prisoners, will need to be retained (further discussed in Section 3-2-2 below). This inflexibility will count against the ability of the operators and the government to come to an arrangement that is more performance-based, because operators will desire base payments that cover (or mostly cover) the requirements imposed by the contract. The limits of competition and marketisation in the prison system are discussed in the next section.

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43 For a confronting look at how incentives to cut service costs can cause private prisons to become unsafe, see Shane Bauer, "My four months as a private prison guard," *Mother Jones*, July/August 2016, accessed 12 February 2019. <https://www.motherjones.com/politics/2016/06/cca-private-prisons-corrections-corporation-inmates-investigation-bauer/> Bauer describes how prisoner supervision, time out of cells, and reintegration services are scaled back when service delivery is the only (or main) lever available to operators for maintaining their profit margins. The prison that Bauer worked in operated on a model in which the operator received a flat payment per prisoner per day, so profited whenever its spending per prisoner per day was less than the payment.

## 3. Competition

One of the primary benefits of privatisation is to inject competition into the prison system, which leads to increased innovation and accountability. The idea here is to create competition between operators for the opportunity to run prisons, and to create competition between them in how they run their prisons, with the intention of lowering the costs of incarceration and improving reoffending results. However, there are natural constraints on competition between prisons and between prison operators: the fundamental rights of prisoners, including the right to equal treatment under the law, along with the situation of private prisons within a system that has governance, priorities, and overheads that individual prisons cannot control, mean that prison operators cannot pursue incentives freely.

The purpose of this section is to discuss reforms that would enable greater competition while respecting these constraints. The tension between justice's need for consistency and competition's need for innovation shapes the kinds of targets and measures that should be used—there is no point setting targets if prisons cannot chase them. In short, there is a difference between privatisation and marketisation; by itself, privatisation may not lead to a competitive market in prison services, and it is competition that drives improved results.

### 3-1. Competition in procurement

**Recommendation 5:** Measures for services linked to recidivism should be standardised across public and private prisons within a system to enable comparisons.

The most obvious way to inject competition into the prison system is through the procurement process. Running a competitive procurement process need not result in privatisation. Many governments have independent agencies that are permitted to bid for the right to operate prisons. Australian examples include:

- In 2016, the New South Wales government announced that it would run a “market testing” process for the operation of John Morony Correctional Centre. Bids were received from three private providers and from Corrections New South Wales. The in-house bid was successful.<sup>44</sup>

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<sup>44</sup> Department of Justice, “CSNSW named as preferred bidder for John Morony Correctional Centre,” Media release, 25 May 2017, accessed 12 February 2019. <https://www.justice.nsw.gov.au/Pages/media-news/media-releases/2017/CSNSW-named-as-preferred-bidder-for-John-Morony-Correctional-Centre.aspx>

- Western Australia's Economic Regulation Authority has recommended that the prison sector be opened up to increased competition between public, for-profit, and not-for-profit providers, noting that competition does not mean privatisation and that the department should determine on a case-by-case basis which organisation is best placed to run a particular prison based on a tendering system.<sup>45</sup>
- Queensland previously had a government-owned corporation that was permitted to compete for contracts; however, this practice was discontinued in 1999 after only two years, apparently under political pressure from unions.<sup>46</sup> The recent decision by Queensland to take back control of its private prisons is a further move away from this model. The state opposition noted again a union influence on this decision.<sup>47</sup>

This process, also known as 'commissioning' or 'competitive neutrality' has been criticised on the grounds that there is little evidence from other jurisdictions that commissioning models increase efficiency, and that in any event the system lacks the data that would be required to make such a model work.<sup>48</sup> On the other hand, in the United Kingdom, the performance of public and private prisons has converged, at least as far as can be told from the available data. Privatisation has been credited with improving the performance of the public sector.<sup>49</sup>

The success of the in-house bid in NSW was taken by opponents of private prisons to be a vindication of the public system.<sup>50</sup> Another way of viewing the result is as a vindication of the competitive process. However, it would not be surprising if, given the concerns about the lack of reliable comparative data, the competitive process was far from perfect, and not yet leading to improved results across the board. As Harding writes, "Without benchmarks private procurement is impossible".<sup>51</sup> This is so because the only way that the parties can know whether a contract is agreeable is if both understand what is being bought and what is being sold.

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45 Economic Regulation Authority, *Inquiry into the efficiency and performance of Western Australian prisons: final report*, 2015. Available here: <https://www.erawa.com.au/inquiries/completed-inquiries/2014-inquiry-to-consider-the-efficiency-and-performance-of-wa-prisons> p. 10

46 Harding (2001), as above, p. 312

47 Vujkovic, as above

48 Jane Andrew, Max Baker, and Phillip Roberts, *The cost of commissioning: research report on the proposed reforms to Western Australian prisons sector*, The University of Sydney Business School, 2015. Available here: <https://www.erawa.com.au/cproot/13826/2/A%20Submission%20in%20Response%20to%20the%20ERA%20Draft%20Report%20-%20Andrew,%20Baker,%20Roberts.pdf> The WA review, which is the subject of this paper, admits that the implementation of commissioning would have to be the last step in the reform process, being enabled by the establishment of measures and data collection and management processes – Economic Regulation Authority, as above, pp. 10-11 On 'competitive neutrality' see Volokh (2013) pp. 370-2

49 Le Vay (2016), as above, p. 257

50 Jesuit Social Services, *Outsourcing community safety: can private prisons work for the public good?*, October 2017. Available here: <http://jss.org.au/wp-content/uploads/2017/11/Private-Prisons-Position-Paper-2017-FINAL.pdf> p. 8

51 Harding (2001), as above, p. 295

The need for reliable measures directly affects state attempts to reduce recidivism. While, as noted in Section 2, it is possible to create simple targets for recidivism itself, a number of other factors that are relevant to reducing recidivism, like education and healthcare outcomes, may not admit such a possibility.<sup>52</sup> What is needed, then, to fully harness the possibility of using private prison contracts to target recidivism are reliable measures that are consistent across all prisons within a given system.<sup>53</sup>

## 3-2. Competition in operations

Along with the need for private and public prisons to be judged by the same standards, competition within the operations of the prison system depends on two further considerations: an appropriate level of transparency, properly applied; and an appropriate level of autonomy for prison operators.

### 3-2-1. Transparency

**Recommendation 6:** Results and costs should be publicly reported.

Critics of prison privatisation often cite transparency as a paramount concern. Andrew, Baker, and Roberts note that “a general lack of transparency” makes it hard to assess the performance of Australia’s private prisons.<sup>54</sup> Jesuit Social Services similarly notes an “almost universal lack of transparency”.<sup>55</sup> Table 3 above demonstrates that the exact governance arrangements of private prisons are very hard to discern most of the time. Given that prison privatisation is often promoted on the basis of lower cost for the same quality, it is legitimate to demand that such assertions are backed with data.

There is, however, a worthwhile question to address: transparency about what? The terms of contracts and internal operations matters are often not disclosed to the public as they are deemed to be commercial-in-confidence. Private prison operators do not want to help their rivals, and this is fair enough if government’s aim is to enable a competitive environment. Moreover, as noted by the Centre for Independent Studies’ Anastasia Glushko, while prison operators do not in general publicly reveal their true

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52 The discussion here sets to one side the possibility that with proper outcome incentives, complex performance indicators like this may not be necessary or useful. That is, that it would be better to simply eliminate altogether indicators like ‘percentage of prisoners involved in education or training’. This is set aside because, right now, indicators like this are standard and as such they are important, though imperfect, inputs into the evaluation of competitive tenders. Once there is a history of direct attempts by prisons to reduce recidivism, this may be a less important consideration.

53 Governments are alert to the need to achieve standardisation of measures across their system. Achieving this standardisation was one of the goals of the ERA review of WA prisons (p. 2, as above). A 2018 VAGO review of private prisons in Victoria also notes that prisons are judged by different standards and recommends improved reporting across the system (pp. 7-13, cited below). The QAO review of Queensland private prisons recommends that government “compares and contrasts the operating standards of public and private prison” (p. 6, cited below). See also the discussion of the new contract for Parklea prison in Section 1, and in fn 44 below. Victorian Auditor-General’s Office, *Safety and cost effectiveness of private prisons*, March 2018. Available here: <https://www.audit.vic.gov.au/sites/default/files/2018-03/20180328-Private-Prisons.pdf> Queensland Audit Office, *Management of privately operated prisons*, Report 11: 2015-16. Available here: <https://www.qao.qld.gov.au/reports-parliament/report-11-2015-16-management-privately-operated-prisons>

54 Andrew, Baker, and Roberts 2015, as above p. 1

55 Jesuit Social Services, as above p. 1

operating costs, they do provide this information to governments.<sup>56</sup> The demand for transparency often seems like a demand that private prison operators act as though they are not, in fact, for-profit enterprises, even though that is precisely the attraction of involving them in the system in the first place.<sup>57</sup>

American academic Jerry Z. Muller argues that transparency can sometimes undermine government by inhibiting debate; the more exposed people are to public scrutiny, the less likely they are to share their ideas and information. Muller argues that we should distinguish between inputs into decisions and the outputs from those decisions. It is the latter that should be made transparent.<sup>58</sup>

In practice, this means that we should be more concerned about the costs of the contracts signed, being the output of the procurement process, and the results obtained by providers, being the outputs of the decision to outsource operations to them. The measures by which costs and results are determined should also be public. Transparency of factors like government deliberations before going out to tender, the preparations of bids, the tender process, and internal operations decisions about how to meet targets, are all less important for ensuring the public interest.

The publication of costs and results, combined with the development of system-wide measures, should allow government to rank prisons by performance. The United Kingdom and New Zealand already have 'league table' systems for prisons, which grade all prisons on universal criteria and show the results side-by-side for comparison.<sup>59</sup> The new contracting arrangements put in place in New South Wales for Parklea and the new Grafton facility are also intended to facilitate greater comparability between private and public prisons (as noted in the fact box in Section 1 above), with Corrective Services New South Wales informing the Legislative Council that it intends to begin publishing a "prison performance league table".<sup>60</sup>

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56 Anastasia Glushko, "Doing well and doing good: the case for privatising prisons," *Policy* 32(1), Autumn 2016 p. 21

57 Setting aside the possibility that not-for-profit enterprises may one day be involved in the operation of prisons.

58 Jerry Z. Muller, *The tyranny of metrics*, Princeton University Press, 2018 p. 161

59 Ministry of Justice, "Prison performance ratings 2017 to 2018," accessed 12 February 2019. <https://www.gov.uk/government/statistics/prison-performance-ratings-2017-to-2018> Department of Corrections, "Prison performance tables," accessed 12 February 2019. [https://www.corrections.govt.nz/resources/research\\_and\\_statistics/prison\\_performance\\_tables.html](https://www.corrections.govt.nz/resources/research_and_statistics/prison_performance_tables.html)

60 Portfolio Committee No. 4 – Legal Affairs, as above (fn 12) Andrew and Baker appeared before the committee and recommended that private prisons' results against KPIs and the fees paid to them for their performance should be publicly reported. Professor Gary Sturgess of the University of New South Wales, also an adviser to Corrective Services New South Wales, made a similar recommendation. (p. 56) GEO supported the introduction of a league table system, in part because the current system imposes greater accountability standards on private prisons than those operated by the state. (p. 58)



### 3-2-2. Autonomy

**Recommendation 7:** Within systemic constraints, prison autonomy should be increased.

The challenge for government, then, is to find the right level and type of transparency that enables public scrutiny and comparison between prisons without compromising the ability of prison operators to manage themselves as commercial entities. Prisons are privatised on the premise that for-profit companies will deliver efficiency, and, in a performance-based regime, quality gains by operating in their own interests. It follows that they must be able to determine their own interests.

Part of this is allowing prison operators scope to determine how they achieve the agreed-upon targets. One of the Wiri (New Zealand) prison consortium's partners has noted that it is important for contracts not to be too prescriptive, so that operators can pursue the incentives on offer. "[G]ive us the freedom to design the solution," Olivier Brousse, CEO of consortium partner John Laing Group, told Citylab in 2017.<sup>61</sup> Similarly, the contract for Melaleuca prison in Western Australia was criticised by that state's Inspector of Custodial Services for being "overly aspirational and highly prescriptive". The Inspector recommended that "Any future revision of the contract should simplify and focus on delivery of outcomes, rather than prescribing how outcomes are achieved".<sup>62</sup>

It must be acknowledged that there are irremovable constraints on the autonomy of prisons. They are not free, of course, to simply treat prisoners however they like; the basic rights of prisoners are not void just because prisoners' liberty has been reduced. Prisons are also constrained by their situation within prison systems. There are not separate public and private systems, and so private prisons have to conform to governance arrangements that make it possible for departments to oversee their operations. This 'systemness' means that not all risks and costs are transferred to private prison operators, and to the extent this is the case, they should neither gain autonomy nor assume responsibility for matters over which they have no rightful control.

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<sup>61</sup> Sharma Rani, as above

<sup>62</sup> Office of the Inspector of Custodial Services, *Inspection of Melaleuca Remand and Reintegration Facility*, April 2018. Available here: <https://www.oics.wa.gov.au/wp-content/uploads/2018/06/Report-117.pdf> p. 9 The experience at Melaleuca is indicative of how prison privatisation can go wrong. Less than 18 months after its opening, the government had to intervene after the Inspector of Custodial Services found that there was a shortfall in the services offered at the prison. Two weeks later, the WA Prison Officers' Union alleged that facility staff had been instructed not to use 'Code red' announcements in order to avoid contractual penalties. Sodexo denied this had happened. This event shows how a poorly-designed contract can cause harm: by being both demanding and imprecise, the contract worked against the interests of both parties. See: Phil Hickey, "Abysmal, bewildering: new report raises concerns with women's prison," *WA Today*, 30 June 2018, accessed 12 February 2019. Phil Hickey (2018) "'Disaster waiting to happen': emergency meeting held at WA women's jail" *theage.com.au* 13 July 2018, accessed 12 February 2019.

Moreover, there is a tension between recommending standardised metrics and greater autonomy. As Muller argues, standardisation runs counter to the development of the kind of local, particular knowledge that is usually required for problem-solving.<sup>63</sup> This is another reason why it is vital that the state seeks to limit measurement to outputs as much as possible. But it also suggests that measures should be developed in concert with providers, and that providers should consult their staff about what is possible and what might work. The goal should be to align local understandings of what is possible with the needs of the system.

Put a different way, the product offered needs to be matched to the wishes of the buyer, and the buyer has to understand, and want, what is available. Privatisation should also mean marketisation. Governments must remember that they are participants in the market, they do not create or command the market. This concern is discussed in the context of costs and the other goals of criminal justice in the following section.

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<sup>63</sup> Muller, as above, p. 49

## 4. The case for the reform

### Key points:

- Government-set performance targets are difficult for free-market policymakers. The desire to use competition to improve performance and lower costs is in tension with the government taking upon itself the role of shaping what a market produces and in what quantity.
- However, the government's natural monopsony in criminal justice gives it a strong position to negotiate favourable terms. Moreover, incentives for reduced recidivism are simple to design and over time a picture of whether and which prison programs are effective will emerge, allowing the attribution of reward and responsibility for recidivism to prisons.
- The primary reason for supporting incentives for reduced recidivism incentives is that the current system is failing. The risk private prisons will make the situation worse if they pursue a reduction in recidivism seems small as against the known outcomes of the current system.
- Targeted reform is needed as an alternative to more radical approaches to addressing the failures of the criminal justice system.

### 4-1. Problems with government targets

For free-market policymakers, privatisation combined with performance incentives of the type discussed in the previous section reveals an uncomfortable truth. There is a tension between performance-based privatisation and the economic reality that technocratic schemes are based on the dubious ability of government to design and monitor targets and measures for whole sectors of the economy. As Muller notes, the setting of performance targets by government mimics one of the features of command economies. When the government sets targets for production, it takes upon itself the task of deciding what should be produced and in what quantity. In a proper market, this is not something the government can determine, since aggregate supply and demand is the product of individual decisions that it cannot anticipate. Premeditated targets distort production, leading supply and demand to become disconnected, resources to become misallocated, and decision-making to become skewed towards satisfying government rather than satisfying local preferences.<sup>64</sup>

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<sup>64</sup> Muller, as above, p. 61-3 – this is standard Hayekian analysis, based on the distribution of knowledge in society.

This argument finds some support in recent experience with government target setting. A 2015 review of the United Kingdom's use of 'payment by results' found that such schemes carry costs and risks that are often underreported. Designing sophisticated contracts can be costly, and their enforcement depends on greater expenditure on reporting and monitoring. Contracts need to offer incentives that are high enough to attract providers, but not so high that taxpayers could end up spending more for a service than is necessary. Incentives need to be tied to exceeding the level of performance that taxpayers could expect without the service. Additionally, while privatisation based on performance passes some operational risks onto service providers, the government retains the risks entailed by the scheme not working or service providers failing to deliver on their promises. The review recommended that performance contracts be limited to use in the delivery of services where results are readily measurable and clearly attributable to actions taken by service providers.<sup>65</sup>

The question, then, is whether this analysis amounts to a dispositive case against incentives for the performance of prison operators, or whether there is something about prisons, and about the proposed incentives, that offsets these concerns.

## 4-2. Can incentives for recidivism reduction work?

The creation of incentives for privately-run, publicly-owned institutions implies that those institutions, left to their own devices, will naturally pursue different targets. This reasoning animates one of the more salient criticisms of private prisons, which is that prison operators have a natural disincentive to correct the behaviour of criminals: they do not benefit from prisoners being released, but they do benefit from released prisoners returning to prison. Viewed this way, the setting of targets is an implicit concession that what is created by privatisation may not actually be a market, properly understood, because actors in the market are not pursuing their own ends but rather ends chosen for them.

In the case of prisons, there are two important points that need to be made in respect of this analysis. The first is that it does not capture all of the various purposes of incarceration, as noted in Section 1. The decision to imprison an offender is also based on the desire to remove that person from the community to prevent him or her from further offending (*incapacitation*), the desire to inflict a proportional amount of harm on offenders in return for the harm they have caused society and their victims (*punishment*), and the desire to discourage crime (*deterrence*). These are also valid aims of incarceration and easily align with the purposes of private providers: if you are running a prison, it is in your interest to keep the prisoners locked inside the prison, thereby incapacitating them, and, since deprivation of liberty is a punishment, the natural operation of a prison achieves this goal as well. And to the extent that punishment deters criminal actions, private prisons achieve this end as well. If private prison providers can provide these services at a lower cost to taxpayers, this is a

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<sup>65</sup> National Audit Office, *Outcome-based payment schemes: government's use of payment by results*, 19 June 2015. Available here: <https://www.nao.org.uk/report/outcome-based-payment-schemes-governments-use-of-payment-by-results/>

positive good, because the state is morally obliged to minimise the burden it places on taxpayers and, more specifically, because increasing resources for incarceration can come at the expense of other parts of the criminal justice system, like policing. Indeed, while it is impossible to measure such a trade-off precisely, we can say even a private prison that performs somewhat worse than the public system in reducing recidivism may nonetheless contribute to public safety if it saves money and contributes to the cost of meeting other public safety priorities.

Secondly, when it comes to contracting out service delivery, the government is in the unusual position of being the only buyer in the market. In this situation, governments have monopsony power. As the only buyers, they have greater scope to dictate terms to sellers looking to expand their operations.<sup>66</sup> In the case of prisons, this leverage is strengthened by the fact that the state has ownership of the relevant assets and a demonstrated ability to run prisons (with a bureaucracy standing ready to do so), meaning that it does not have to find an outside buyer if it does not find one it likes. While the terms of the contract are bound by feasibility (as noted, there is no point going to market for something that it is not possible to supply), governments do have the ability to describe what their expectations of sellers are, and thus to shape the product. This means that a target for reducing recidivism is not as artificial as it might first appear. On the other side of the negotiating table are companies that have already sunk capital into establishing their ability to operate prisons, meaning that they are strongly incentivised to find and develop new market opportunities.

Note, however, that the first of these points is an argument for privatisation of government services where it is cost-effective, rather than an argument for trying to shape the operation of those services towards other pre-determined ends. And the second point rests on the empirical claim that the government's sole buyer status is actually exploitable in that way. It is possible that just because a market exists in imprisonment, this does not mean that a market in corrections (as in, reducing recidivism) is possible or feasible.

Indeed, the Brookings Institution has found that prison privatisation in the US has failed to create a competitive market in corrections, and attributes to this failure the lack of evidence for private prisons delivering better service than public prisons.<sup>67</sup> Reviewing the UK system, Le Vay also suggests that the reforms in that country have been disappointing in this respect.<sup>68</sup>

In part, the cause of these failures is that government's monopsony power is not absolute. While prison operators are capital-committed to the business of running prisons, they are also, almost invariably, large multinationals with diversified interests, and, in general, they do not own the prisons they operate. This means that they do

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<sup>66</sup> David Youngberg, "How to fix private prisons," Foundation for Economic Education, 8 June 2017, accessed 12 February 2019. <https://fee.org/articles/how-to-fix-private-prisons/>

<sup>67</sup> Megan Mumford, Diane Whitmore Schanzenbach, and Ryan Nunn, *The economics of private prisons*, The Hamilton Project, Brookings Institution, October 2016. Available here: <https://www.brookings.edu/research/the-economics-of-private-prisons/>

<sup>68</sup> Le Vay, as above, pp. 259-261



have the ability to withdraw their capital from the market in prison services and pursue more profitable endeavours. In practice, this has meant that prison operator contracts are long-term, reducing the power of the state to exploit its advantages, and are mostly focused on operations rather than outcomes. This explains why, for example, the Ravenhall contract's performance component is only 2.5 percent of the fees paid by government.

And, as noted in Section 3-2-2 above, the market in corrections is constrained not only by the nature of the seller, but by the nature of the buyer: the state has certain specifications that it must include in corrections contracts in order to deliver on its other promises to citizens. That is, government cannot allow its desire to see corrections made more efficient and effective to trump its other interests in justice and whole-of-government costs.

### **4-3. Reasons for performing the experiment**

If it is the case that government target-setting confronts inherent economic complications, that we have good reason to believe that a market in corrections (as opposed to a market in imprisonment) is necessarily constrained by the nature of both buyer and sellers, and the overall record of private prisons on costs is mixed (as outlined in section 1, above), the ultimate question is why ought governments to pursue, as they seem to be doing, the incentivisation of recidivism reduction.

The single best argument for taking this experimental approach is, to put it bluntly, the terrible performance of all prisons, public and private, in correcting criminal behaviour. None of the above concerns change this key fact: on average almost half of prisoners in this country will return to prison within two years of being released, while more than half will reoffend within that timeframe. Philosophical concerns about the utility of aggregate measures will not address what strikes most as common sense. As a society we are paying for prisons that, while effective in removing offenders from our streets, are putting many of those same offenders back into the community unchanged or even more likely to commit crime than they were before. While it is valid to note the risk that the experiment leads to even worse results, this argument is really an argument for making sure that as much of this risk as possible is transferred to private providers. In any event, there is little evidence to suggest that results will be worse, given what is known about the current situation.

Couple this with the reality that private prisons have existed for a long time in Australia, remain under long-term contracts, and will be increasing in number in the short-term, and it seems obvious that government should pull whatever levers it can to promote private operators' participation in addressing the high rate of recidivism.

Moreover, recidivism seems like a sound candidate for an experiment of this type. As discussed in Section 3-1, it is easy to measure recidivism. A baseline for performance is not required; a bonus can be attached directly to each individual prisoner.<sup>69</sup> It is

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<sup>69</sup> Though note again the contents of fn 30, above.

true that it is less straightforward to attribute success or failure to the prisons involved—prisons might get a number of false positives or negatives that mislead them as to the success of their policies and innovations—but this is offset by the participation of the operators in the negotiations of the scale of the incentives and, moreover, it is likely to become less of a problem over time as programs are tested and refined. While equal justice places a natural limit on how diverse the approaches of various prisons can be, other concerns, such as the free choice of participants, are less pronounced in prisons than they are in some other contexts, like public health interventions or specialised education curriculums. Unlike the populations affected by those government interventions, the prison population has effectively opted-in—by committing crime in the first place.

Finally, as ever, there is a more radical proposal on the table. Pointing to high costs, high recidivism, and high representation within the prisoner population of some racial and cultural minorities, radical activists have recently begun agitating for the abolition of prisons altogether. The goal of these activists is not necessarily the overnight closure of all prisons, but rather a gradual ‘decarceration’ through the expansion of alternatives to prison, the adoption of a therapeutic mentality towards crime and criminals and a sociological analysis of supposed structural inequalities that are held to create crime, and the further integration of criminal justice and the welfare state.<sup>70</sup> There is, of course, considerable merit in reducing the number of nonviolent offenders who go to prison—as previous IPA research has shown, the most serious offence of up to 46 percent of prisoners in Australia was a nonviolent offence, there are real lessons our country should take from the experience of some American states, Indigenous incarceration does interact in complex ways with cultural and demographic phenomena, and there are ways to improve our non-prison punishments that stand a good chance of succeeding.<sup>71</sup> However, the notion of abandoning incarceration altogether is undesirable and infeasible. Despite their problems, prisons are very effective in incapacitating offenders and imposing just punishment upon them. Important questions about who merits this treatment and how prisons can better serve the interests of justice and public safety do not change this reality.

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70 For example, see: Paul Gregoire, “A world without bars: the prison abolition movement,” *Sydney Criminal Lawyers*, 29 April 2017, accessed 12 February 2019. <https://www.sydneycriminallawyers.com.au/blog/a-world-without-bars-the-prison-abolition-movement/> Joshua Dubler and Vincent Lloyd, “Think prison abolition is impossible? It once felt inevitable,” *The Guardian*, 19 May 2018, accessed 12 February 2019. <https://www.theguardian.com/commentisfree/2018/may/19/prison-abolition-america-impossible-inevitable> German Lopez, “The case for abolishing prisons,” *Vox*, 19 June 2017, accessed 12 February 2019. <https://www.vox.com/policy-and-politics/2017/6/19/15764176/prisons-abolition-alternatives> John Washington, “What is prison abolition?” *The Nation*, 31 July 2018, accessed 12 February 2019. <https://www.thenation.com/article/what-is-prison-abolition/> Nayuka Gorrie and Witt Church, “We need to abolish prisons to disrupt a society built on inequality,” *The Guardian*, 26 November 2018, accessed 12 February 2019. <https://www.theguardian.com/commentisfree/2018/nov/26/we-need-to-abolish-prisons-to-disrupt-a-society-built-on-inequality>

71 Andrew Bushnell and Daniel Wild, *The use of prisons in Australia: reform directions*, Institute of Public Affairs, December 2016. Available here: <https://ipa.org.au/publications-ipa/research-papers/the-use-of-prisons-in-australia-reform-directions> Andrew Bushnell, *Criminal justice reform: lessons from the United States*, Institute of Public Affairs, April 2017. Available here: <https://ipa.org.au/publications-ipa/research-papers/criminal-justice-reform-lessons-united-states> Andrew Bushnell, *Indigenous Australians and the criminal justice system*, Institute of Public Affairs, September 2017. Available here: <https://ipa.org.au/publications-ipa/research-papers/indigenous-australians-criminal-justice-system> Andrew Bushnell, *Making community corrections work*, Institute of Public Affairs, May 2018. Available here: <https://ipa.org.au/publications-ipa/research-papers/making-community-corrections-work>

For anyone interested in defending traditional standards of criminal justice, reform of the prison system is vital. The problems of the system are known and will not solve themselves, and, left unattended, invite a more radical response. In its waning days, the administration of President Barack Obama announced that the US federal prison system would no longer use private prison operators, citing underperformance on services and costs.<sup>72</sup> This is a demonstration of the instability of the status quo.

It is this context that makes the experiment in using the power of contracts to reduce recidivism worthwhile. The important caveat that cost, feasibility, and lack of competition make its success far from certain remains. However, private prisons remain a possible contributor to solving this key problem in the criminal justice system, not just because the current system is not working, but because, in the end, prison operators have an interest in satisfying their customers—namely, the taxpaying public whose most basic demand is the safety of their families and communities.

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<sup>72</sup> Sally Yates, Memorandum for the *Acting Director Federal Bureau of Prisons*, US Department of Justice, 18 August 2016. Available here: <https://www.justice.gov/archives/opa/file/886311/download>

# Conclusion

Australia makes extensive use of private prisons, though the sector has seen little growth in the last two decades. Our country also has a rapidly increasing prison population and a high rate of recidivism. It is natural then to consider what contribution private prisons can make to improving corrections and community safety. In recent years, governments here and overseas have begun experimenting with new contractual incentives for private prison operators, aimed at encouraging them to invest more in services designed to reduce recidivism.

There are reasons to be sceptical about whether this experiment will succeed. The top-down creation of performance incentives and the retention by government of a substantial interest (namely, justice) in the prison system both argue against the formation of a true market in reducing recidivism. The mixed performance of private prisons on costs and service delivery seems to support this worry. But there are, of course, very sound reasons for making the attempt: the problems that we see in the system now merit our attention and the government begins negotiations with private providers in a strong position.

Following the recommendations made in this report will give the experiment the best chance of succeeding. Recidivism incentives should be bonuses rather than penalties, to encourage innovation, and they should be tied to each individual prisoner so that the risks involved are out in the open. Similarly, where there are indirect incentives for reduced recidivism, such as targets for the delivery of services correlated with reduced recidivism, these should be based on measures that are standardised across the system, to enable comparisons and competition. The costs and results should be publicly reported. The point is to create competition between bidders for operations rights and between prisons themselves. A competitive process need not lead to greater privatisation—if the threat of privatisation forces underperforming public prisons to improve, then this should be welcomed. But so too should be greater privatisation if that is what results merit. If the premise of the reform is that it is the results that count, then the entire system needs to buy into that priority.

Private prisons can continue to play a prominent role in Australia's prison systems by viewing this experiment as an opportunity. If they can win their bonuses for reducing recidivism, they will boost their margins and satisfy their customers. They will also contribute to reforming the lives of offenders. This is the win-win-win on offer: better prisons, safer communities, and renewed human dignity.

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## Arthur Gorrie

### Information

*At the time of writing, Arthur Gorrie is run by GEO Group:*

GEO Group Australia, "Arthur Gorrie Correctional Centre: Serving the courts, managing risk," accessed 11 February 2019. <https://www.geogroup.com.au/arthur-gorrie-correctional-centre.html>

*At the time of writing, both Arthur Gorrie and Southern Queensland Correctional Centre are under tender (though see notes for Southern Queensland Correctional Centre below):*

Tom Gillespie, "Tender open for privately-run prison in Lockyer Valley," *The Chronicle*, 2 January 2018, accessed 11 February 2019. <https://www.thechronicle.com.au/news/tender-open-privately-run-prison-lockyer-valley/3302171/>

## Southern Queensland Correctional Centre

### Information

*Serco has operated this facility as a men's prison, with a reported capacity of 300 men (Gillespie, as above). It has been announced that the facility will be converted to a women's prison.*

Minister for Police and Minister for Corrective Services, "Media statements," 3 July 2018, accessed 11 February 2019. <http://statements.qld.gov.au/Statement/2018/7/3/189-cells-commissioned-at-borallon-training-and-correctional-centre>

*As reported by the ABC, there has been some confusion regarding the operation of this facility going forward, with the tender process suspended in the middle of 2018 pending an investigation by the Crime and Corruption Commission.*

Catherine Van Extel, "Serco marketing privately run maximum security women's jail to Queensland inmates, advocacy groups says," ABC News, 16 August 2018, accessed 11 February 2019. <https://www.abc.net.au/news/2018-08-16/serco-marketing-privately-run-prison-to-queensland-inmates/10124310>

## Mount Gambier

### Information

Department for Correctional Services, "Mount Gambier Prison," accessed 11 February 2019. <https://www.corrections.sa.gov.au/prison/prison-locations/mount-gambier-prison>

G4S Australia and New Zealand, "Mount Gambier Prison," accessed 11 February 2019. <http://www.au.g4s.com/what-we-do/care-justice-services/justice/mount-gambier-prison/>

### Contract

Tenders SA, "Contract for the management and operation of Mount Gambier Prison," accessed 11 February 2019. <https://www.tenders.sa.gov.au/tenders/contract/download.do?id=8535&section=contract>

*Under the contract, the state may withhold part of the operating fee if performance targets are not met (Cl 19.2) and there are a number of charge events detailed in Schedule 8.*

## Acacia

### Information

Department of Justice, "Acacia Prison," accessed 11 February 2019. <https://www.correctiveservices.wa.gov.au/prisons/prison-locations/acacia.aspx>

### Contract

Department of Justice, "Acacia Prison contract," accessed 11 February 2019. <https://www.correctiveservices.wa.gov.au/about-us/business-with-us/tenders-contracts/acacia-prison-contract.aspx>

*Payments are set out in Schedule 2. It is worth noting that both the formulas and amounts to be paid are publicly available.*

## Melaleuca

### Information

Department of Justice, "Melaleuca Remand and Reintegration Facility," accessed 11 February 2019. <https://www.correctiveservices.wa.gov.au/Prisons/prison-locations/melaleuca.aspx>

*The innovative bonus model of the Melaleuca contract was touted by the Western Australian government when the prison opened in 2016.*

Courtney Bembridge, "New Perth women's prison opens with cash incentives for successful rehab," ABC News, 18 December 2016, accessed 11 February 2019. <https://www.abc.net.au/news/2016-12-18/new-womens-prison-opens-in-perth-with-operator-offered-incentive/8130394>



# CUTTING COSTS AND REDUCING REOFFENDING REDESIGNING PRIVATE PRISON CONTRACTS FOR BETTER RESULTS

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## About the author

**Andrew Bushnell** is a Research Fellow at the Institute of Public Affairs, working on the Criminal Justice Project. He previously worked in policy at the Department of Education in Melbourne and in strategic communications at the Department of Defence in Canberra.

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